

## Message Text

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PAGE 01 HELSIN 01139 240747Z

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SUBJECT: COST OF PRODUCTION INSURANCE

REF: (A) STATE 99922 (B) 83421 (C) USMISSION OECD PARIS 9326

1. SUMMARY: DETAILS OF FINLAND'S COST OF PRODUCTION INSURANCE SCHEME (K-GUARANTEES) ARE GIVEN. RISING COST OF SCHEME AND SOCIAL DEMOCRATIC PARTY IDEOLOGICAL OBJECTIONS CAUSED GOVERNMENT IN APRIL 1974 TO REVISE ELIGIBILITY CRITERIA. HOWEVER, SCOPE OF SCHEME MAY BE INCREASED SOON TO COVER MAJOR CONSTRUCTION PROJECTS IN EASTERN EUROPE. A COMMISSION IS STUDYING EXPORT GUARANTEE PROGRAM INCLUDING K-GUARANTEES AND WILL MAKE RECOMMENDATIONS AT END OF 1975. END SUMMARY.

2. FINALAND'S EXPORT GUARANTEE BOARD (VIENTITAKUULAITOS OR VTL) WAS ESTABLISHED BY EXPORT GUARANTEE ACT OF SEPTEMBER 14, 1962. IT CHIEFLY ADMINISTERS POLITICAL AND COMMERCIAL RISK INSURANCE PROGRAM IN SUPPORT

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PAGE 02 HELSIN 01139 240747Z

OF FINNISH EXPORTS. IT ALSO ADMINISTERS, USING

PROFITS OF RISK INSURANCE AND DIRECTLY APPROPRIATED TREASURY FUNDS, THE "KUSTANNUSTASO" (COST-LEVEL) OR "K-GUARANTEE" PROGRAM, UNDER WHICH COST OF PRODUCTION INSURANCE IS SOLD TO PRODUCERS OR EXPORTERS OF FINNISH INDUSTRIAL PRODUCTS, FOR SPECIFIC CONTRACTS OF AT LEAST 18 (AT FIRST 12) MONTHS DURATION (60 MONTH MAXIMUM).

3. K-GUARANTEES ARE SOLD FOR A PREMIUM OF 0.01 PERCENT PER MONTH OF THE TOTAL VALUE OF THE CONTRACT. AT THE CONCLUSION OF THE CONTRACT PERIOD, IF THE BUREAU OF STATISTICS WHOLESALE PRICE INDEX OF DOMESTIC INDUSTRIAL PRODUCTS HAS RISEN BY AT LEAST 11 (AT FIRST 7) PERCENT PER ANNUM, THE VTL PAYS AN INDEMNITY, CALCULATED TO REIMBURSE APPROXIMATELY 60 PERCENT OF THE INCREMENTAL COST DUE TO INFLATION IN EXCESS OF 11 PERCENT, NOT THE TOTAL INFLATION-INDUCED COST INCREASE.

4. IN APRIL 1974, THREE CHANGES WERE MADE, TO RESTRICT THE BENEFITS OF THE SYSTEM TO LARGE CONTRACTS, AND TO REDUCE THE SUBSIDY ELEMENT. THE MINIMUM TERM OF ELIGIBLE CONTRACTS WAS RAISED FROM 12 TO 18 MONTHS. THE BASE LEVEL OF INFLATION WAS RAISED FROM 7 PERCENT TO 11 PERCENT PER ANNUM, TO MORE ACCURATELY REFLECT AVERAGE DOMESTIC INFLATION, AS WELL AS THE AVERAGE INFLATION IN FINLAND'S MARKETS AND IN ITS COMPETITORS' PRODUCTION COSTS. ALSO THE MINIMUM INDEMNITY WHICH WOULD BE PAID WAS RAISED FROM 1000 TO 10,000 FMK. (FROM 280 TO 2800 DOLLARS). THE MAIN REASONS FOR THE CHANGES WERE RISING COSTS AND POLITICAL OPPOSITION, CHIEFLY BY SOCIAL DEMOCRATS, TO STATE EXPORT ASSISTANCE PROGRAMS, AS TOO GENEROUS TO BUSINESS. FYI: IT WAS AT THIS TIME LAST YEAR THAT SOCIAL DEMOCRATIC PARTY DEMANDS FOR COUNTER-CYCLICAL DEPOSITS FROM THE WOOD-PROCESSING INDUSTRY WAS A MAJOR POLITICAL ISSUE. END FYI.

5. BECAUSE OF THE MINIMUM CONTRACT PERIOD REQUIREMENT, THE K-GUARANTEES HAVE BEEN EFFECTIVELY LIMITED TO THE HEAVY METALS INDUSTRY, PRIMARILY THE SHIPBUILDING AND WOOD PROCESSING EQUIPMENT INDUSTRIES. THE GUARANTEES LIMITED OFFICIAL USE

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PAGE 03 HELSIN 01139 240747Z

HAVE BEEN PROVIDED WITHOUT REFERENCE TO THE BUYER, AND IN PRACTICE ARE ABOUT 50 PERCENT FOR SALES TO MARKET ECONOMIES AND ABOUT 50 PERCENT FOR SOCIALIST COUNTRIES, CHIEFLY THE USSR (SHIPS).

6. THE AMOUNT OF EXPORTS COVERED BY THE K-GUARANTEE PROGRAM, AND DELIVERED IN 1973 WAS 872.8 MILLION FMK, OR 6.0 PERCENT OF THE TOTAL 1973 EXPORTS OF

14,605 MILLION FMK. IN 1974, 1,783.5 MILLION FMK OF EXPORTS WERE COVERED, 8.6 PERCENT OF THE TOTAL 20,687 MILLION FMK. VTL ESTIMATES THAT IN 1975 OVER 2,000 MILLION FMK OF EXPORTS WILL BE COVERED. SINCE THESE FIGURES REPRESENT CONTRACTS WRITTEN IN THE EARLY 1970'S, THE BULK OF THE INCREASE IN VALUE OF EXPORTS COVERED REPRESENTS INCREASES IN THE NUMBER OF CONTRACTS, PARTICULARLY FOR SHIPS.

7. A DECISION, AS YET NOT OFFICIALLY ANNOUNCED, BUT "VIRTUALLY CERTAIN" ACCORDING TO A VTL DIRECTOR, TO INCLUDE THE MAJOR CONSTRUCTION PROJECTS IN EASTERN EUROPE, PARTICULARLY THE USSR, IN THE K-GUARANTEE SYSTEM WILL GREATLY INCREASE THE COSTS, ALREADY PROJECTED AT AS MUCH AS 1.75 BILLION FMK FOR 4-YEAR PERIOD 1975-8, BY THE SECOND MINISTER OF FINANCE, A SOCIAL DEMOCRAT. (VTL CONSIDERS THIS FIGURE TOO HIGH, BUT CALCULATION DEPENDS ON UNPREDICTABLE FUTURE INDEX LEVELS). THE 1974 PAYOUT WAS 150.5 MILLION FMK, A SUBSTANTIAL INCREASE OVER THE 41.8 MILLION FMK NET PAYOUT IN 1973.

8. THE SYSTEM IS AGAIN UNDER ATTACK, BECAUSE OF RISING COSTS AND FOR POLITICAL REASONS, AND A COMMISSION HAS BEEN APPOINTED TO STUDY THE EXPORT GUARANTEE PROGRAM, WITH PARTICULAR ATTENTION TO THE K-GUARANTEES, IN THE CONTEXT OF THE GOVERNMENT'S EXPORT-EXPANSION INVESTMENT PROGRAM AND RELATED BALANCE OF PAYMENTS MEASURES. A REPORT IS DUE AT THE END OF 1975.

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